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Trade Promotion Council of India
Notified in the Foreign Trade Policy by Department of Commerce, Government of India

Forex Market Insights

Newsletter

Volume 08 → Apr 30th to May 06th 2022

Welcome

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Dear Stakeholders,

The Chinese Yuan directed Asian currencies this week after weakening to 6.65 against the US dollar, with oil rising amid Moscow cutting off gas supplies to Poland and Bulgaria. As Yen and Euro hit 20-year and 5-year lows respectively, the dollar is flying high on hopes of a 0.5% rate hike at the May 4 Fed meeting, as the interest rate gap increases between these economies. Recessionary fears loom as US economy contracted first time in 2 years.

Locally, the much awaited LIC IPO is finally opening on May 4, albeit with a lower stake sale, as market participants expect to see a gush of Dollar inflows in this offering. Rupee almost headed towards it low but a probable intervention from RBI capped the US$INR pair. Is RBI expected to follow Fed's footsteps in raising rates in June policy? No amount of speculation will turn the table and only time will tell.

Regards

Mr Vijay Gauba
Additional Director General
Trade Promotion Council of India

Key Takeaway Summaries

₹ INR

LIC IPO is opening on May 4,. On the last trading day, rupee inclined towards the positive zone..

€ EUR

EUR/US$ regains some levels after falling 2.30% in the week but the heavy monthly deprivation amounted to 4.68%.

£ GBP

It is estimated that BOE will raise interest rate by 25 bps, BOE is open to an aggressive hawkish stance due to rising inflation.

¥ JPY

Bank of Japan pledged to defend its zero rate policy with unlimited govt. bond purchases.

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₹ INR

REPO RATE	GDP	INFLATION	UNEMPLOYMENT	TRADE BALANCE
4.0%	1.84%	6.95%	8.1%	$-18.51B

Events to WATCH

May 02, 10:30
Nikkei Markit Manufacturing PMI (Apr)

May 02, 16:30
Federal Fiscal Deficit (Mar)

May 02, 17:30
Trade Balance

May 05, 10:30
Nikkei Services PMI (Apr)

The US$/INR pair ended the week at 76.42. The pair saw pressure mostly all over the week and traded above 76.50. But with the LIC IPO finally opening on May 4, the rupee inclined towards a positive zone on the last trading day. The global sentiment indicates that the rupee withstood the pressure above 103 paise. Next week, all eyes will be on the FOMC meeting. This makes a lot of sense considering that the US$ is strengthening over almost all other currencies and of course, the rupee represents an emerging market economy.

Furthermore, there are a lot of tensions about global growth slowing down, and the strengthening US$ acts as a bit of a feedback loop as emerging market debt is denominated in US$. So it creates some concern for countries like India. The events to watch next week are Nikkei Markit Manufacturing PMI (Apr), Federal Fiscal Deficit (Mar), Trade Balance and Nikkei Services PMI (Apr). Important data points due out for the US are JOLTs Job Openings (Mar), ADP Nonfarm Employment Change (Apr), Fed Interest Rate Decision, Crude Oil Inventories, Initial Jobless Claims and Non-farm Payrolls (Apr).

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$ USD

REPO RATE	GDP	INFLATION	UNEMPLOYMENT	TRADE BALANCE
0.5%	-1.4%	8.5%	3.6%	$-89.18B

Events to WATCH

May 02, 19:30
ISM Manufacturing PMI (Apr)

May 03, 19:30
JOLTs Job Openings (Mar)

May 04, 17:45
ADP Nonfarm Employment Change (Apr)

May 04, 19:15
Markit Composite PMI (Apr)

May 04, 23:30
Fed Interest Rate Decision

May 05, 18:00
Initial Jobless Claims

Range bound trades in US$/INR continued for the second consecutive week with the fulcrum around 76.50-76.60. Despite dollar index surging to its highest levels since Jan 2017, the rupee held its ground. Earlier this week, Rupee weakened to 76.77, its lowest since 9 Mar 2022. Let's peek into the daily candlestick chart for some clues. The region of 76.77 – 76.97 (red horizontal lines), has been established as a strong dollar resistance zone. It has warded off two attempts in successive months. There are 2 long standing price gaps yet to be filled: 74.73 (23 Feb'22) to 75.0225 (24 Feb'22) – blue horizontal lines, and 73.9750 (13 Jan'22) to 74.04 (14 Jan'22) – purple horizontal lines. It's quite unusual because price gaps in US$/INR gets filled up. An upward moving trend line (pink color), connecting the dollar lows of 73.7725 (12 Jan'22), 74.535 (23 Feb'22) and 75.31 (5 Apr'22) comes around 75.80-75.90. This region could be an important short-term support. After a steady uptick, two momentum indicators, viz. MACD and RSI have cooled off towards the neutral territory. Another momentum indicator, Slow Stochastic is still in the overbought zone. Technically, we could see the US$/INR pair cooling off towards the support region of 75.80-75.90. Exporters can continue to increase their hedge ratios at spot above 76.50-60. Use forwards as the preferred hedging instrument and some vanilla options to diversify risk. Importers can target spot around 75.80 – 76.00 to restart hedging. Use an optimum mix of vanilla options and forwards to hedge. Vanilla option premiums will be moderate/low despite high risk premium due to increased economic & geo-political uncertainties.

€ EUR

REPO RATE	GDP	INFLATION	UNEMPLOYMENT	TRADE BALANCE
0.0%	0.2%	7.5%	6.8%	€-7.62B

Events to WATCH

May 02, 11:30
German Retail Sales (MoM) (Mar)

May 02, 13:30
Manufacturing PMI (Apr)

May 03, 13:25
German Unemployment Change (Apr)

May 04, 11:30
German Trade Balance (Mar)

May 04, 13:30
Services PMI (Apr)

May 04, 14:30
Retail Sales (MoM) (Mar)

EUR/US$ breaks four days of falling trend and maintains levels above 1.05 amidst a risk aversion sentiment. Since 2015, the EUR/US$ has recorded the biggest loss of 4.75% in the month of April 2022. Although substantial losses have been recorded on Wall Street, a sudden change in sentiment failed to push the dollar against the euro. US Core PCE was down marked, but headline inflation rose to 6.6%, as the monetary policy meeting will be held in May by FOMC. The EUR/US$ regained some levels after falling down 2.30% in the week but the heavy monthly deprivation amounts to 4.68%, quite pertinent since January 2015. The week ended with gloomy market sentiment. US equities witnessed heavy losses, between 2.77% and 4.17%. Covid outbreak in China threatened to derange supply chains. US Central bank rate hikes and the Ukraine-Russia situation were factors influencing the last trading session of the month.

The Euro has seen a massive loss in value during the previous week to reach the 1.05 level. This region is a large, round, psychologically historically important support handle, hence a little amount of shorts unwinding seen there. Although, nothing on this chart suggests that a turnaround might happen in the near future. Hence, trades which seem more likely are rallies that we can short, and the daily chart could be a good indicator for that. Based on the current price action the 1.08 level above should be a significant resistance handle. Presently we can very likely expect “fading rallies”, as traders continue to heavily favor the greenback. A fact to remember is that the ECB is very dovish, while the Federal Reserve remains very hawkish. As long as the divergent central bank policies hold, it does make sense that we would see market participants favor the US dollar. Furthermore, we’re amidst a risk on situation, and that almost always favors the US dollar. There is no good reason to think that things are going to suddenly shift in the current situation, and therefore the Euro should eventually go higher. If we rally to break above the 1.08 level, there is still a lot of noise above there that could cause problems.

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£ GBP

REPO RATE	GDP	INFLATION	UNEMPLOYMENT	TRADE BALANCE
0.75%	1.3%	7.0%	3.8%	£-9.26B

Events to WATCH

May 03, 14:00
Manufacturing PMI (Apr)

May 05, 14:00
Services PMI (Apr)

May 05, 14:00
Composite PMI (Apr)

May 05, 16:30
BoE Interest Rate Decision (May)

May 06, 14:00
Construction PMI (Apr)

GBP/US$ fell 1.9% this week, Pair made a low of 1.24 last week, which we have seen 22 months ago amid dollar index reached its highest level in 20 years, just close to 104 due to Fed rate hike anticipations. The CME's Fed Watch tool indicated a 96.5% probability of a 50 basis points rate hike next month and a 85% chance of a 50 basis points hike in June as well. We expect a rebound in sterling from current levels as the pair will be heavily influenced by the BOE'S decision due next week. The BOE is expected to raise interest rates by 25 bps. The BOE is open to an aggressive hawkish stance due to rising inflation in UK. It's quite an important week for the pair as Manufacturing PMI of April is scheduled in the start of week itself while Composite & Services PMI are set to release in the mid of week. Market participants will be eying the release of Non-farm payrolls which is expected to come 51k lower.

The British pound has lost its value significantly in the previous trading week. This is a region that will continue to cause quite a lot of volatility, but one has to be cautious in the current situation because this market looks like it is about to fall apart. Rallies will almost certainly appear, but they should be thought of as opportunities to short the pound and go long dollar. If we break below the previous week's low, it is likely that we test the 1.225 handle. Rallies at this point will incur a lot of resistance at every major level, and the 1.30 level above will almost certainly be a offer massive resistance. Until we break above the 1.30 level that I would think there isn't a real chance to turnaround. In fact, we are starting to form the so-called "death cross" on the weekly chart, so we believe it is probably only a matter of time before traders will focus on where the bottom could be.

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¥ JPY

REPO RATE	GDP	INFLATION	UNEMPLOYMENT	TRADE BALANCE
-0.10%	1.1%	1.2%	2.6%	¥-412B

Events to WATCH

May 06, 05:00
Tokyo Core CPI (YoY) (Apr)

US$/JPY ended the week almost 1% higher at 129.83. Pair went to a high of 131.24 and went as low as 126.93. Japanese currency fell to a 2 decade low on Thursday as the Bank of Japan pledged to defend its zero rate policy with unlimited govt. bond purchases and Fed rate hike expectation in May and June also aided dollar gains. There is less expectation of the Yen appreciating in upcoming days. It’s quite an important week on the economic side, as Japan will be closed for 3 days in next week due to local holidays. Manufacturing PMI of April month is set to release on Monday. Market participants will be eying the release of Nonfarm payrolls which are expected to come 51k lower compared with previous print of 431k..

The Japanese yen depreciated against the dollar as the Bank of Japan maintained its base rate at -0.1% and promised to defend its yield curve with unlimited purchases of 10-year JGBs. The MACD has been over 2 continuously for more than 2 weeks. There are few examples of such dominance in the last 30 years. The RSI has been overbought for a long time & hovering above 70. The first resistance is at 130. If the pair breaks it which is very likely, the second resistance is at 131.25. The first support can be seen at 128.33 followed by the second at 126.94. The FOMC Wednesday meeting could put pressure on the pair. If the Fed follow a 0.25% surge rather than 0.5% or delays the beginning of balance sheet reduction, chance of a pair reaction is quite high.

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BLOG

Foreign exchange rate system evolution

The forex rate exchange rate regimes that are prominent today didn't exactly start the way they exist now. Initially, before the inception of foreign exchange markets, the gold standard was the norm where the value of a country's currency was tied to the gold it possessed. The effect of keeping inflation in check was served by the value of money backed by a fixed asset-gold. However, this standard limited the competitive advantage of countries that didn't hold abundant gold reserves and failed to consider businesses and individuals' value resourcefulness to an economy. Thus, the US ended the Gold standard in 1971. In a failed attempt to revive fixed exchange rates, US President Richard Nixon temporarily suspended the dollar's convertibility to gold in 1971. By March 1973, with the inception of major currencies floating against each other, the modern foreign exchange market started its shift from a fixed exchange rate to a floating exchange rate system.

Thus, a global decentralized, over the counter (OTC) market for trading currencies evolved, determining forex rates for each currency. The evolution of the fixed and floating exchange rate system witnessed new emergences and many downfalls over the years ranging from the International Gold Standard during 1875-1914 to the Bretton Woods System during 1945-1972 to morph into the foreign exchange system prevalent today. The shift has been noticed in not just the evolving systems but also preferences of countries and its outlook towards the pegged and floating exchange regime with the development of economies and trade.

While during the mid-1970s, a massive chunk of countries, amounting to nearly 83%, had some sort of pegged exchange rate, the 1990s observed the gravitation of economies towards the floating exchange rate system. Depending upon whether the foreign currency exchange rates fluctuate constantly or not, there are two types of exchange rates: fixed and flexible exchange rates. The government of a country can allow market forces and economic conditions to determine the rate of conversion, or the government can fix a rate by pegging the value of their currency with a stronger and stable currency of another country. No consensus has been reached regarding the perfect foreign exchange rate regime for an economy as the benefits a country gets would be dependent on characteristics like inflation rate, magnitude of financial development, size of the economy, capital mobility, etc.

Fixed Exchange Rates

The official rate set and maintained by the government is the fixed or pegged foreign exchange rate. A country holds forex reserves in order to sustain the determined pegged rate agreed between participating countries and thus witnesses buying and selling of its own currency by the Central Bank in the forex market. In a country with fixed exchange rates, the home currency's value is pegged to a major world currency that enables, especially, for weaker economies to benefit from stimulated trade and greater certainty of navigation against adverse market movements and an upper hand in terms of forex risk management.

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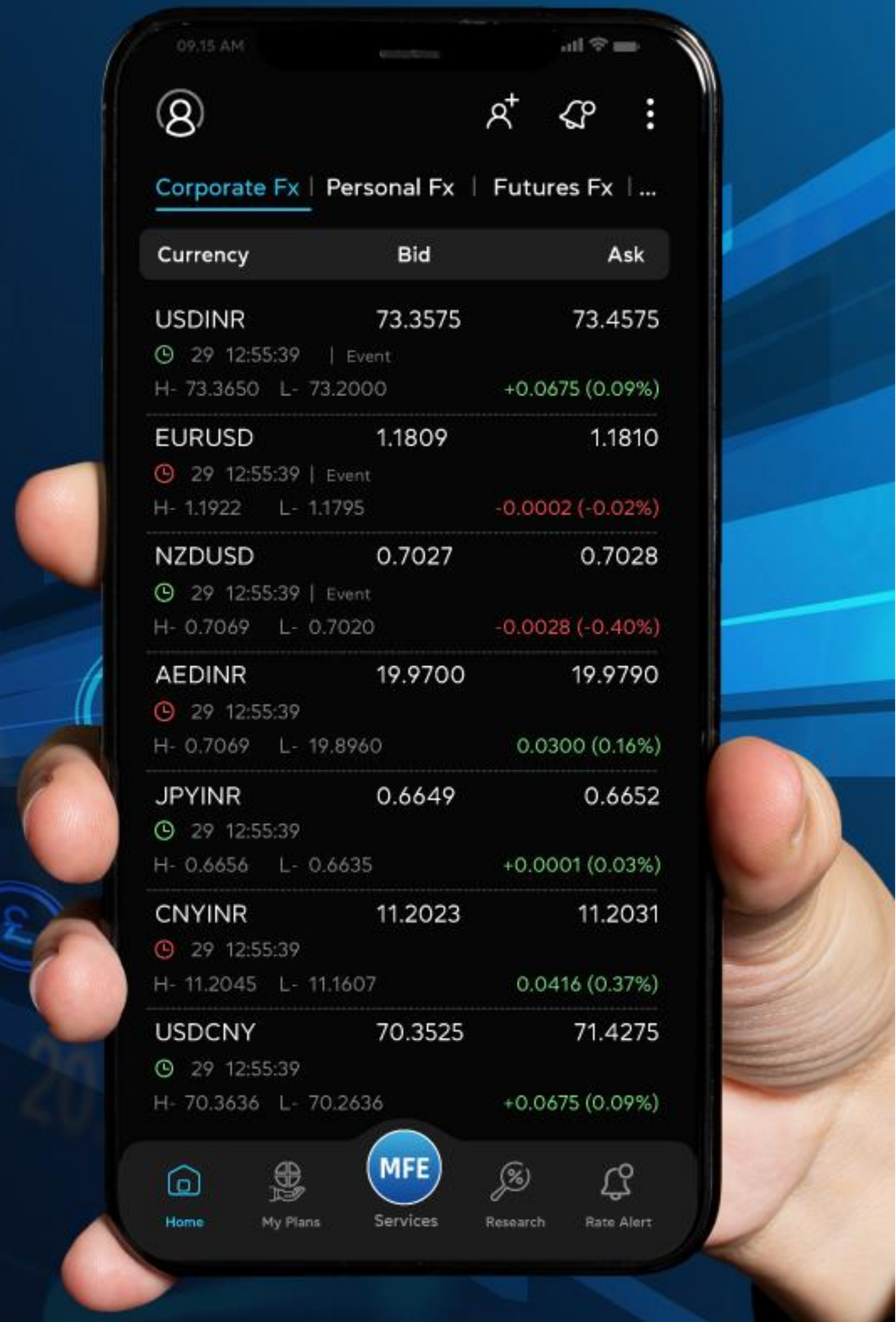

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TPCI Trade Promotion Council of India

Contact Details

Myforexeye
Simplifying Forex

Ritik Bali
8860447723
advisory@myforexeye.com

TPCI Trade Promotion Council of India
Notified in the Foreign Trade Policy by Department of Commerce, Government of India

Nikhaar Gogna
9818995401
editorial@tpci.in

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